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Cybertek Computer Products, Inc. v. Whitfield et al.

No. 23911

Appellate Department, Superior Court of California, Los Angeles County

1977 Cal. App. LEXIS 2140; 203 U.S.P.Q. (BNA) 1020

November 21, 1977

PRIOR HISTORY: [*1]

Action by Cybertek Computer Products, Inc., against Pinckney Whitfield, and Tracor Computing Corporation, for trade secret misappropriation. Judgment for plaintiff.

LexisNexis(R) Headnotes**COUNSEL:**

Martin R. Horn, Wayne Willenberg, and Spensley, Horn, Jubas & Lubitz, all of Los Angeles, Calif., for plaintiff.

Donnelly, Clark, Chase & Johnson, Los Angeles, Calif., for defendants.

OPINIONBY:

TITLE

OPINION:

Title, Judge.

This matter was submitted on October 27, 1977, and the Court herein proposes to render judgment as follows:

I.

In this action for injunctive relief and damages arising out of alleged misappropriation by defendants of confidential information and trade secrets in connection with plaintiff's computer software system, the Court has bifurcated the issue of liability from that of damages pursuant to stipulation of the parties, and has now concluded the trial of the liability issue. Except for the issues relating to the existence of confidential information and trade secrets in relation to said system, the extent to which such confidential information or trade secrets were and are being used by defendants, as well as some additional related issues, the facts are basically uncontroverted and have been [*2] set forth in the stipulated factual statement of the parties heretofore filed in this action.

Very briefly, and by way of an overview without attempting to set forth the facts in any considerable detail, the dispute essentially arises out of the prior employment of defendant Whitfield by plaintiff, and his subsequent employment by defendant Tracor in the same field of endeavor. Plaintiff was formed in 1969 for the purpose of engaging in the business of furnishing computer related services to the life insurance industry. Defendant Whitfield was one of the founding officers of plaintiff, and had a substantial background and expertise in computer software, as specifically related to its use in the life insurance business. He purchased shares in plaintiff, and in his capacity as an employee of plaintiff, directly participated in the design and development of plaintiff's on-line new business computer system known as the Auto/Issue System, his responsibilities including the specific design of some major portions of the system. For a time he had management responsibility for this system, and subsequently was a senior analyst involved in its design, programming and testing.

In connection [*3] with his employment, defendant Whitfield executed an Employee Nondisclosure Agreement, dated December 2, 1970, which provided among other things that the techniques and methods relating to plaintiff's products were trade secrets and confidential, and that he would not at any time disclose to anyone outside of plaintiff any information about plaintiff's products which related to the design, use or development of such products. The agreement specifically made reference to the Auto/Issue System. He voluntarily terminated his employment and relationship with plaintiff on March 31, 1971, at which time he acknowledged in writing that he understood his agreement with plaintiff not to disclose confidential information, and that he had returned all confidential material to plaintiff. He thereafter did some consulting work for defendant Tracor between July and October, 1971, commenced full-time employment with said defendant on November 15, 1971, and ever since that time has remained in said defendant's employ. His duties with defendant Tracor have included respon-

sibility for the development of an insurance on-line new business system, which would provide substantially the same capabilities [*4] as plaintiff's Auto/Issue System, and which was to be marketed in direct competition to plaintiff's Auto/Issue System.

Plaintiff developed its Auto/Issue System over a period of approximately two years, from November, 1969 through approximately November, 1971. Since that time it has been marketing the system. Defendant's similar system, which it has named Trac/70, has been substantially though not completely developed, but is nevertheless being marketed at the present time in competition with plaintiff's Auto/Issue System. It was stipulated by the parties that plaintiff and defendant Tracor have each expended in excess of \$500,000 in the development of their respective systems.

II.

Plaintiff has at all times maintained and enforced a corporate policy which requires its employees to execute Employee Nondisclosure Agreements such as that executed by defendant Whitfield, and which further requires its potential and actual licensees to execute nondisclosure agreements prior to receiving Auto/Issue documentation other than marketing material. Plaintiff also at all times herein maintained additional reasonable measures of security which clearly demonstrate plaintiff's [*5] intention to keep information concerning its products, including the Auto/Issue System, confidential, such as the marking of documentation relating to its products as confidential, the use of registration numbers in connection with copies of its documentation, and permitting only authorized personnel to have access to its Auto/Issue documentation other than marketing materials. Defendant Tracor has likewise taken similar steps relating to security in order to protect the confidentiality of its on-line new business system known as Trac/70.

III.

It is plaintiff's contention that during defendant Whitfield's consultations and employment with defendant Tracor, he has been substantially and directly involved in the design of said defendant's Trac/70 System, in connection with which he has utilized and disclosed plaintiff's trade secrets and confidential information in violation of his duty to plaintiff, and in breach of his specific Nondisclosure Agreement with plaintiff. Both defendants deny any responsibility to plaintiff, and contend that the alleged trade secrets and confidential matter claimed by plaintiff are in fact not trade secrets or confidential, but rather are well known [*6] concepts in the computer industry, that they are, therefore, not confidential, and that defendant Whitfield has merely utilized his substan-

tial degree of skill and experience in his employment by defendant Tracor which he had developed prior to his employment with plaintiff and which he has the right to so utilize.

IV.

There are a number of basic threshold issues to be determined by the Court, which appear to involve mixed questions of law and fact. Among these are the following: Do any or all of the 12 items set forth in plaintiff's Exh. 1A (said exhibit purports to enumerate the areas of design and development of the Auto/Issue System which constitute the confidential information and trade secrets concerning which plaintiff is entitled to protection), or any combination thereof, constitute confidential information or trade secrets? If they fail to reach the dignity of trade secrets, do they nevertheless constitute confidential matter entitled to protection under the law? Is the nondisclosure contract executed by defendant Whitfield with plaintiff a valid and binding agreement? What was the intention of the parties under said nondisclosure agreement? Was any of said alleged [*7] confidential matter or trade secrets disclosed by defendant Whitfield to defendant Tracor in connection with the development of the Trac/70 System?

V.

While there may have been a question in the past as to whether or not computer software is susceptible of protection under the trade secret doctrine, it is clear that such protection is available today in practically all jurisdictions. See 38 George Washington Law Review 909, and cases cited by both plaintiff and defendants in their respective trial briefs, all of which make it amply clear that computer software is protectable under the trade secret doctrine, given appropriate facts and circumstances.

IV.

It should be noted at the outset that plaintiff and defendant Whitfield executed a document entitled "Cybertek Employee Non-Disclosure Agreement" on December 2, 1970, which as already indicated purports to restrict the disclosure by defendant Whitfield of certain information concerning plaintiff's products, including the Auto/Issue System. Plaintiff places considerable importance on this agreement in this litigation, and defendant Whitfield contends that the agreement is not binding upon him for a number of reasons, including [*8] the contention that the agreement was executed without consideration. While it is true that the nondisclosure agreement was executed a number of months after the commencement of defendant Whitfield's employment with plaintiff, plaintiff contends that this is of no moment because when plaintiff was first formed by its founding officers consisting of Vaughn Morgan, Nancy Wilten and defendant Whitfield, it was

clearly understood and agreed that the on-line new business system which would be developed by plaintiff would be confidential and not disclosed to any outsiders without the necessary controls to insure the confidentiality of such system, and that the subsequent execution of the written nondisclosure agreement was only to memorialize their prior oral agreement. A consideration of all of the evidence leads the Court to conclude and find these to be the true facts, and that, therefore, the contention of a lack of consideration must fail. The evidence demonstrates without question that from the very inception, it was always the intention of said principals that their development of the Auto/Issue System would be considered to be highly confidential matter, and this is supported [*9] not only by the said nondisclosure agreement of December 12, 1970, but also by the agreement executed with Pacific Mutual Life Insurance Company as well as the agreement with I.S.A., both of which contained language clearly indicating such confidentiality.

The contention has also been advanced by defendants that said nondisclosure agreement is violative of the Public Policy of California, as articulated in *Section 16600 of the Business and Professions Code*. Defendants cite no authorities to support this position. A distinction must be drawn between contracts which prohibit an employee from competing with his former employer, which subject to certain exceptions do violate said Business and Professions Code section, and agreements which seek to prohibit an employee from disclosing confidential information and trade secrets, which do not come within the ambit of said section. See *Gordon v. Londau*, 49 Cal.2d 690, and *Winston Research Corp. v. Minnesota Mining and Mfg. Co.*, 350 F.2d 134 at page 140, 146 USPQ 422, at 426. Thus, the Court concludes that the nondisclosure agreement is valid and binding upon defendant Whitfield.

VII.

Said nondisclosure agreement is not ideally drafted, [*10] and leaves some room for interpretation. Plaintiff concedes that it was not its intention to prohibit the disclosure of any and all information relating to its products, but only such information which would reasonably be deemed to be confidential or in the nature of a trade secret. The Court agrees with this interpretation, and finds that the parties intended by said agreement to prohibit defendant Whitfield from disclosing any information concerning its products which would reasonably be deemed confidential to the point where it should not be revealed to outsiders without some contractual control and limitations. The Court does not believe or find that the parties intended any distinction between the use of the words "trade secrets" on the one hand and "confidential" on the other hand, but rather used these terms interchangeably

to indicate information which should reasonably be withheld from outsiders. Thus the task of the Court will be to determine whether the nondisclosure agreement, so interpreted, has been violated by the defendant Whitfield during his employment by Tracor.

VIII.

The Court having concluded that the nondisclosure agreement is indeed a valid and subsisting [*11] agreement, it is necessary to determine the effect of said agreement in the factual context of defendant Whitfield's activities on behalf of defendant Tracor. A fair reading of the cases would seem to indicate that considerable importance is placed upon the existence of such contracts, as compared to situations where no agreement exists between the employer and his former employee. See *Futurecraft Corp. v. Clary Corp.*, 205 C.A.2d 279, where in denying relief to the plaintiff on the trade secrets theory, the court pointed out that the trial court had found that there was no agreement of nondisclosure between the employer and the employee, and further cited in support of its position the case of *Wexler v. Greenberg*, 160 A.2d 430, 125 USPQ 471 where relief was also denied, one of the grounds again apparently being that there was no express covenant between the parties relating to nondisclosure of the confidential information. There is a clear inference from both of these cases that relief may well be denied in the absence of a covenant of nondisclosure between the parties. While the existence or nonexistence of such a contract is not determinative, and relief may under some circumstances [*12] be granted even in the absence of a contract, the existence of a contract makes it more probable that the employer will be granted relief for breach of contract, and this may be so even if the confidential information, knowledge or technology, does not rise to the dignity of a trade secret. *Structural Dynamics Research Corporation v. Engineering Mechanics Research Corporation*, 401 Fed.Supp. 1102 so held, and specifically pointed out that a former employee may be liable for breach of contract if he uses confidential information gained while employed with a former employer, even though such information was not itself a trade secret. In view of these cases, the Court has concluded that considerable weight must be given to the fact that plaintiff and defendant Whitfield executed the nondisclosure agreement in question.

IX.

The above observations of the Court must lead to the conclusion that if confidential matter relating to the Auto/Issue System was disclosed by defendant Whitfield to defendant Tracor, particularly if that confidential matter was in the nature of trade secrets, liability would have to be imposed. Considerable time was expended during the course of trial by counsel [*13] in an effort to de-

lineate the difference between confidential matter on the one hand and trade secrets on the other hand, but at least in the factual context of this case, this may amount to a distinction without a difference, and in the Court's view a proper disposition of this case does not necessitate the drawing of such a fine line.

X.

Simply stated, plaintiff's position is that some 12 areas of development and design in its Auto/Issue System set forth in extremely technical language in Exh. 1A constitute trade secrets, or at least highly confidential matter which should be protected either on the theory that defendant Whitfield breached his confidential duty to plaintiff or breached his express covenant of nondisclosure. To determine this issue, it is necessary to attempt to glean a definition of a trade secret from the authorities and case law, and that examination of the authorities and cases makes it immediately obvious that while the simplistic definitions found therein are easily understood, the application thereof to a highly technical area such as computer software programs is extremely difficult. Section 757 of the Restatement of Torts, Comment b, generally defines [*14] a trade secret as any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it. In spite of this simple definition, it further states that an exact definition of a trade secret is not possible, and list some factors to be considered in determining the existence or nonexistence of a trade secret. Briefly stated, these include the extent to which the information is known by others outside of the business or employees of the business, the extent of measures taken to guard the secrecy of the information, the value of the information, the effort and expense involved in developing it, and lastly the ease or difficulty with which the information could be properly acquired or duplicated by others. As to some of the latter factors, plaintiff clearly comes within their ambit, as the evidence is virtually uncontradicted that reasonably strict security measures were taken to guard the secrecy of the Auto/Issue System, in excess of \$500,000 was expended by plaintiff to develop it, license fees of somewhere between \$100,000 and \$200,000 are charged plaintiff's customers [*15] for the right to use the system, and a formidable and expensive task is faced by any competitor who might desire to properly acquire or duplicate it. The serious conflict in the evidence arises, however, in connection with the factor dealing with the issue as to the extent to which the information is known to others outside of plaintiff's business. Defendants essentially contend that we are not dealing with trade secrets, nor for that matter even confidential matter to any degree, because all the alleged items set forth in Exh. 1A are not

secret or confidential information but rather consist of well known concepts in the computer and data processing industry, and consequently cannot be any stretch of the imagination be considered confidential or secret. This issue was joined in the traditional battle of the experts, with Dr. Gilbert and others testifying on behalf of plaintiff to the effect that Exh. 1A indeed did include unique and confidential approaches not known to the computer industry in general, and Mr. Shafto and others testifying on behalf of defendants to the contrary. The technical nature of their testimony would be mind boggling to the average lay person, as it was [*16] to the court, and this is amply demonstrated by the fact that Mr. Shafto, an obviously well qualified expert in the computer field, testified that he had great difficulty in even understanding the meaning of the descriptive language of the alleged trade secrets found in Exh. 1A. The Court has carefully considered all of the testimony, and has concluded that at least to some degree, defendants' position is correct in that some of the approaches utilized in the Auto/Issue System, standing separately, are general concepts known to experts in the computer industry. The cases indicate, and plaintiff concedes that general concepts are not protectable, per se, as trade secrets. However, the cases further indicate that while general concepts are not protectable, the specific implementation involving a particular combination of general concepts may well amount to a trade secret. See *Winston Res. Co. v. Minnesota Mining & Mfg. Co.*, *supra*, involving the manufacture of a tape recording device, supporting this theory. That court pointed out that the same general concepts had been used in developing defendants' machine as had been used in plaintiff's machine, that such development involved [*17] the use of general concepts and approaches which were known in the industry, and were, therefore, not in and of themselves susceptible of trade secret protection. However, the court further pointed out that while the general approach and the basic mechanical elements thereof were not trade secrets, that the specifications of these basic mechanical elements and their relationship to each other embodied in plaintiff's machine were not publicly known, were arrived at only after painstaking research and extensive trial and error, and, therefore, constituted a trade secret entitled to protection. In other words, the court found that the specific embodiment of the general concepts and approach into a combination of parts was protectable, even though all or some of them might well be known to the industry. Also see *By-Buk Co. v. Printed Cellophane Tape Co.*, 163 C.A.2d 157, 118 USPQ 550. The Court believes that the principle announced in these cases applies to our case, and that while some of the concepts set forth in Exh. 1A are general concepts not susceptible of protection, that the entire bundle or combination of these concepts as developed and utilized by plaintiff in its Auto/Issue [*18]

System do constitute trade secrets which are protectable under the circumstances. As pointed out in the above mentioned Restatement of Torts, as well as in *80 Harvard Law Review 1432, at page 1452*, any information which provides a competitive advantage over competitors may well constitute a trade secret, and in the Court's view it is obvious that the combination of factors involved in the Auto/Issue System must give the plaintiff its protection under this doctrine.

XI.

Having concluded that the confidential matter in question should not have been disclosed by defendant Whitfield, the next issue which must be determined is whether in fact there was such a disclosure by him in connection with his work on the development of Tracor's Trac/70 System. Defendant Whitfield contends that since he took away no actual documentation or physical material relating to the Auto/Issue System, it must follow that he did not disclose or use any confidential information relating thereto, but rather merely made use of his expertise and general know-how in the development of Trac/70. Putting it in another way, defendants contend that Trac/70 was independently developed, and was not copied from plaintiff's [*19] Auto/Issue System. This presents an extremely close question of fact for the Court to determine, and the Court is not unmindful of the classic confrontation in the law of the policy which strives to extend some protection to an employer from the breach of confidence of a former employee in taking away and utilizing trade secrets with the policy of the law which protects an employee in his right to carry on his trade or profession after he leaves his employer. The Court also has considered the well recognized principle that where a defendant in a trade secret case claims independent development, that the burden then shifts to the defendant and places upon the defendant a heavy burden of persuasion to show that the production was a result of independent development and not from the use of information confidentially secured during the prior employment. This principle has been articulated in many cases, including *Bolt Associates, Inc. v. Alpine Geophysical Associates, Inc.*, 365 Fed.2d 742, 151 USPQ 520.

Looking to the evidence, it is not seriously controverted, and the Court finds that there are in fact substantial similarities in the Auto/Issue System and the Trac/70 System. Such [*20] similarity, while not determinative of the issue, is of obvious importance, and must be given weight. Granted that the systems are not identical, many cases indicate that such identity is not required, and that trade secrets need not be exactly copied in order to impose liability. Likewise, the conceded difference in terminology utilized in the systems is not significant.

Defendants have also argued that many of the similarities are purely coincidental, since there were relatively few options which every expert in the field would consider in arriving at methods of approach for a new business on-line system. However, plaintiff presented evidence to the effect that there were in fact significant design choices, and that similar choices utilized by defendants would, therefore, indicate copying rather than independent development. This again is a question of fact, and the Court accepts Dr. Gilbert's testimony to the effect that there were significant design choices, and not as indicated by defendants, choices only as to insignificant details. Furthermore, even if the Court resolves the conflict in the evidence regarding whether or not defendant Whitfield took away with him documentation [*21] concerning the Auto/Issue System in favor of defendant Whitfield, the cases are clear that documentation need not be taken in order to establish liability, since appropriation by memory alone is proscribed. As pointed out in 38 *George Washington Law Review*, page 909 at pages 938 and 939, the weight of authority indicates that appropriation by memory will be proscribed under the same circumstances as an appropriation via more tangible means.

When the Court considers all of the above factors, and adds thereto the ingredient sustained by the evidence that defendant Whitfield had complete knowledge and understanding of plaintiff's system, and in addition supervised and oversaw the development of defendants' system, the Court concludes and finds that defendant Whitfield did disclose and utilize substantial aspects of plaintiff's Auto/Issue System in the development of the Trac/70 System.

XII.

Defendant Whitfield's liability having been established, the Court must finally determine whether defendant Tracor also has liability under the circumstances. The cases indicate, as does Section 757 of the Restatement of Torts, that a new employer may also be liable for misappropriation of [*22] trade secrets, provided that he utilizes the information with notice of the secret nature thereof and with notice that the employee has disclosed it in breach of his duty to the former employer. See *By-Buk Co. v. Printed Cellophane Tape Co.*, *supra*. The evidence indicates that before any substantial development of the Trac/70 System was begun, defendant Whitfield had been placed on notice by plaintiff by letter concerning a possible trade secret violation, and defendant Tracor was apprised of said demand by defendant Whitfield. In addition, it is conceded by defendants that the instant lawsuit was actually filed before any substantial development of the Trac/70 system. Under these circumstances, the Court finds that defendant Tracor was on notice of the poten-

tial liability in this matter, and consequently the Court finds that defendant Tracor has liability herein along with defendant Whitfield.